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No. 88-710

In the Supreme Court of the United States

OCTOBER TERM, 1988

ORKIN EXTERMINATING COMPANY, INC., PETITIONER

v.

FEDERAL TRADE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the Federal Trade Commission had authority under Section 5(a)(1) of the Federal Trade Commission Act, 15 U.S.C. 45(a)(1), to condemn as an "unfair * * * act[ ] or practice[ ]" the refusal by petitioner to honor more than 200,000 contracts with individual consumers, promising those consumers that petitioner would provide specified termite control services each year at a fixed annual fee.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A211-A249) is reported at 849 F.2d 1354. The opinion and final order of the Federal Trade Commission (Pet. App. A136-A210) and the initial decision of the administrative law judge (Pet. App. A3-A135) are reported at 108 F.T.C. 263.

JURISDICTION

The corrected judgment of the court of appeals was entered on July 15, 1988. A petition for rehearing was denied on September 19, 1988 (Pet. App. A250). The petition for a writ of certiorari was filed on October 28, 1988. The jurisdiction of this court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner is a national provider of pest control and exterminating services (Pet. App. A138, A216). Petitioner typically contracts with consumers to provide termite control services by means of standard printed forms that are not subject to modification by petitioner's agents or customers (*id.* at A216).

In 1966, petitioner began to offer what it called "lifetime" guarantees of continued protection for structures treated for termite infestation. Between January 1966 and February 1, 1975, petitioner's contracts for termite protection and control (the pre-1975 contracts) provided that a customer who had obtained initial inspection and (if needed) treatment for termite infestation could obtain subsequent annual reinspection (and necessary treatment) by paying a fixed annual renewal fee, the amount of which was specified in the contract (Pet. App. A217).

Petitioner's contracts promised to provide that protection for the "lifetime" of the treated structure, unless it was structurally modified (Pet. App. A217-220). Moreover, as petitioner indicated in a 1968 advertising campaign promoting the program, "[t]he yearly premium for this lifetime protection *is very modest and never increases*" (*id.* at A220 (emphasis in original)).

In August 1980 petitioner began notifying more than 207,000 parties to pre-1975 contracts that the company was going to increase its annual renewal fees. Annual fees were raised to a minimum of $25 or by 40%, whichever was greater (Pet. App. A222).

In the face of complaints by customers throughout the country and officials in 17 states, who protested petitioner's attempt to alter the terms of its contracts, petitioner developed what it called an "accommodation program." In addition to rolling back increases for customers

who had entered into contracts in 1968, when petitioner's advertising material specifically guaranteed that there would be no price increases, the accommodation program also permitted representatives of petitioner to rescind increases for other customers who complained about the increases with sufficient precision and tenacity. See Pet. App. A222-224.

As of August 1984, petitioner had, through its "accommodation program," rolled back the renewal fees of 21,500 customers, approximately 16,000 of whom were 1968 customers. Also, more than 42,000 customers had canceled pre-1975 contracts for reasons the record does not reveal. Pet. App. A225. As of August 1, 1984, however, petitioner was still collecting increased annual renewal fees from more than 140,000 customers with pre-1975 contracts and had received increased revenues through 1984 of $7,515,674 (Pet. App. A51, A222).

2. In May 1984, the Federal Trade Commission (Commission) issued an administrative complaint alleging that petitioner's unilateral breach of scores of thousands of consumer contracts constituted an "unfair * * * act[ ] or practice[ ]" in violation of Section 5 of the Federal Trade Commission Act (FTC Act), 15 U.S.C. (& Supp. IV) 45. Following pretrial discovery, Commission "complaint counsel" moved for a summary decision pursuant to Section 3.24 of the Commission's Rules of Practice, 16 C.F.R. 3.24(a). Petitioner filed a cross-motion for summary decision. Pet. App. A225.

The administrative law judge (ALJ) ruled in the Commission's favor. He found that petitioner's pre-1975 contracts did provide for a fixed renewal fee and that petitioner had breached those contracts by increasing the renewal fees. Pet. App. A225. To determine whether petitioner's conduct constituted an unfair act or practice, the ALJ then applied the Commission's three-part test for

finding unfairness.[1] He concluded (1) that petitioner's unilateral breach of thousands of consumer contracts caused substantial consumer injury; (2) that consumers could not reasonably have avoided the injury; and (3) that there were no countervailing benefits to consumers or competition from the challenged conduct. The ALJ's order required petitioner to roll back all fees in pre-1975 contracts to the levels specified in those contracts. Pet. App. A225-A226. On appeal by petitioner, the Commission affirmed the ALJ's decision in all respects (*id.* at A226).

3. On petitioner's petition for review, the court of appeals affirmed and enforced the Commission's order.[2] The court rejected "[petitioner's] suggestion that [its pre-1975 contracts] are silent as to the duration of the stated annual renewal fees" (Pet. App. A230). Rather, the court sustained the Commission's conclusion that petitioner's pre-1975 contracts unambiguously promised lifetime treatment of covered structures at a fixed renewal fee that would not be increased (*id.* at A226-A233).

The court of appeals next reviewed the Commission's application of its three-part test for unfairness. The court concluded that the Commission had properly found that the undisputed facts of this case amply satisfied that test. First, the court noted that by unilaterally breaching more

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[1] The test is as follows (Pet. App. A236):

> To justify a finding of unfairness the injury must satisfy three tests. It must be substantial; it must not be outweighed by any countervailing benefits to consumers or competition that the practice produces; and it must be an injury that consumers themselves could not reasonably have avoided.

See also *American Financial Services Ass'n* v. *FTC*, 767 F.2d 957, 970-971 (D.C. Cir. 1985), cert. denied, 475 U.S. 1011 (1986).

[2] The court issued its opinion on April 19, 1988, and issued a corrected opinion on July 15, 1988. The court's opinion of July 15, 1988, is the one summarized below.

than 200,000 consumer contracts, and collecting amounts in excess of the specified rate on more than 140,000 of those contracts, petitioner had realized more than $7 million to which it was not contractually entitled. Although the loss to each individual consumer was small, the aggregate consumer injury was substantial. Pet. App. A238.

The court also noted that the Commission had concluded that petitioner's unilateral breach of contract provided no countervailing benefits to consumers or competition, because the breach had been unaccompanied by any increase in or enhancement of the services provided to consumers. Petitioner did not challenge that conclusion. Pet. App. A239.

Finally, the court affirmed the Commission's conclusion that consumers could not reasonably avoid the substantial injury caused by petitioner's conduct. The court noted that "[a]nticipatory avoidance through consumer choice was impossible because these contracts give no indication that the company would raise the renewal fees as a result of inflation, or for any other reason" (Pet. App. A240). The court also noted that mitigation of the injury was infeasible because the company's "accommodation program" was not made known to consumers and was available only to those who affirmatively complained about the increase. Likewise, consumers could not mitigate damages by transferring their business to competitors of petitioner because such competitors (who would not have received the economic benefit that petitioner received from making the initial inspection and treatment of a house) would not be willing to offer consumers renewal terms equivalent to those in the contract with petitioner. *Id.* at A240-A241.

Having found that the record supported the Commission's conclusion that its test for unfairness was satisfied, the court then considered petitioner's contention that application of the unfairness standard was improper. The

court held that "[t]he Commission's conclusion * * * that it was an 'unfair' practice to breach over 200,000 contracts * * * was a reasonable application of the Commission's unfairness standard" (Pet. App. A243).

The court noted that the FTC Act expressly prohibits both "unfair" and "deceptive" acts and practices, so that it was not necessary to show deception in petitioner's conduct in order to establish a statutory violation (Pet. App. A244, A246-A247). The court concluded that although this case, with its focus on non-deceptive contract breaches, "may be unprecedented," denial of the Commission's authority to stop the practice "given the extraordinary level of consumer injury which [petitioner] has caused * * * would be inconsistent with the broad mandate conferred upon the Commission by Congress" (*id.* at A245-A246).

In addition to affirming and enforcing the Commission's order, the court of appeals entered an injunction pendente lite pursuant to Section 5(c) of the FTC Act, 15 U.S.C. 45(c), requiring petitioner to desist from implementing further fee increases in violation of the Commission's order, until such time as the order becomes final.[3]

ARGUMENT

The decision of the court of appeals comports with the precedents of this Court and other courts of appeals, recognizing that Congress intended to accord the Commission broad flexibility in construing the meaning of "unfair acts or practices." The Commission reasonably applied its unfairness authority in this case to require that petitioner honor a contractual promise it had made to more than

[3] Commission orders do not become final until all judicial review is complete (see 15 U.S.C. 45(g)).

200,000 consumers. There is no reason for this Court to review the judgment of the court of appeals upholding the Commission's order.

As this Court has repeatedly recognized, Congress deliberately cast the prohibitions of Section 5 of the FTC Act in flexible terms so that the Commission could address the " 'many and variable unfair practices which prevail in commerce.' " *Atlantic Refining Co.* v. *FTC*, 381 U.S. 357, 367 (1965) (quoting S. Rep. 597, 63d Cong., 2d Sess. 13 (1914)); see also *FTC* v. *R.F. Keppel & Bro.*, 291 U.S. 304, 310-311 (1934). Considering the deference that is due an agency's construction of its statute (see, *e.g.*, *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837, 843-844 (1984)), it is not surprising that the Court has cited with apparent approval an earlier administrative definition of "unfair acts or practices" (*FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233, 244-245 n.5 (1972)). The Commission's current three-part test is simply a refinement of that test.[4] It has been applied by other courts of appeals. See *American Financial Services Ass'n* v. *FTC*, *supra*; *Harry & Bryant Co.* v. *FTC*, 726 F.2d 993, 999-1000 (4th Cir.), cert. denied, 469 U.S. 820 (1984). Neither Congress nor any court has suggested that the test misinterprets the FTC Act.[5]

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[4] The Commission's 1964 test for unfairness specified that a practice must meet at least one (but not necessarily all) of the three criteria. Consumer injury was one of the criteria, but the test as then formulated did not explicitly require a showing that the injury was unavoidable, or explicitly require a weighing of the countervailing benefits to competition. It was to allay concern about the potential breadth of the 1964 standard that the Commission formulated the narrower test that was applied in this case. See *American Financial Services Ass'n* v. *FTC*, 767 F.2d at 970-971.

[5] Both Houses of Congress, in fact, have passed bills that would have codified this test, but for reasons unrelated to their definitions of "unfair acts or practices" those bills did not become law. See S. 1078, 99th Cong., 1st Sess. (1985); 131 Cong. Rec. 20765 (1985); H.R. 2385,

Although petitioner suggests that the three-part test applied by both the Commission and the courts of appeals is improper insofar as it results in condemnation of a company's breach of a consumer form contract, petitioner cites no authority for that position. In fact, as the court of appeals observed (Pet. App. A244 (citation omitted)), "[s]ome of the oldest 'unfairness' decisions involve sellers' refusals to live up to the terms of their contract." And even if the Commission has not previously considered the precise type of contractual breach at issue here, petitioner does not even acknowledge the extensive precedent supporting the Commission's authority to refine the concept of "unfair practices" on an incremental basis to address the wide and ever-changing array of potentially injurious trade practices.

As the court of appeals recognized, in this case the Commission "simply [held] that it was an 'unfair' practice to breach over 200,000 contracts" where most consumers were essentially remediless and received no countervailing benefits (Pet. App. A243). Insofar as the court of appeals' opinion establishes that the Commission may act in other instances where companies breach thousands of consumer form contracts at a cost of millions of dollars to consumers, and where no reasonable means exist by which

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99th Cong., 1st Sess. (1985); 131 Cong. Rec. H7503 (daily ed. Sept. 17, 1985); *House Passes, With No Fanfare, FTC's Authorization Bill With Legislative Veto,* 49 Antitrust & Trade Reg. Rep. (BNA), No. 1232, at 483, 485 (Sept. 19, 1985); S. 677, 100th Cong., 1st Sess. (1987); 133 Cong. Rec. S4795 (daily ed. April 8, 1987); H.R. 2897, 100th Cong., 1st Sess. (1987); 133 Cong. Rec. H8276-H8277 (daily ed. October 7, 1987); *Hill Staffs Agree on Some Issues in FTC Reauthorization Legislation,* 54 Antitrust & Trade Reg. Rep. (BNA), No. 1372, at 1143-1144 (June 30, 1988).

consumers may avoid such injury,[6] petitioner does not suggest why such a result is either legally wrong or undesirable as a matter of policy.

Finally, petitioner overstates matters considerably in contending that the court's ruling "exposes all businesses which use consumer form contracts to the threat of * * * severe penalties under federal law for any breach of these contracts" (Pet. 9). This case did not involve just "any breach" of a consumer contract, and any precedent it establishes is clearly qualified by the facts on which the factual finding of unfairness was based. Moreover, the order of which petitioner seeks review requires only that it desist from further overcharging its customers in violation of their contracts, and that it rescind unilateral increases previously imposed in violation of contract terms (Pet. App. A204-A210).[7] Such an order is hardly the kind of precedent that requires this Court's intervention in the absence of any decisional authority to support petitioner's position.

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[6] According to petitioner, the Commission "close[d] its eyes" (Pet. 9) to evidence that means of avoidance were available to consumers. In fact, the Commission carefully considered the evidence (Pet. App. A180-A183). Insofar as petitioner objects to the uniform factual conclusions of the Commission and court of appeals on this point, its request for certiorari contravenes the principle that this Court " 'will intervene only in what ought to be the rare instances when the [substantial evidence] standard appears to have been misapprehended or grossly misapplied.' " *American Textile Mfrs. Inst.* v. *Donovan*, 452 U.S. 490, 523 (1981) (quoting *Universal Camera Corp.* v. *NLRB*, 340 U.S. 474, 491 (1951)).

[7] Should the Commission wish to make petitioner pay back the more than $7 million it has previously collected by dishonoring its contracts or obtain any other relief in the nature of damages, it will be required, as petitioner acknowledges (Pet. 9-10 n.3), to demonstrate in a district court action that petitioner's conduct was that "which a reasonable man would have known under the circumstances was dishonest or fraudulent" (15 U.S.C. 57b(a)(2)).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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